

withdrawable accounts means the aggregate of (i) amounts placed with an institution for deposit or investment and (ii) earnings outstanding on the books of account of the institution at the close of the taxable year which have been credited as dividends upon such accounts prior to the close of the taxable year, except that such term, in the case of a building and loan association, does not include permanent nonwithdrawable capital stock represented by shares, or earnings credited thereon.

(e) *Examples.* The provisions of this section may be illustrated by the following examples:

Example 1. (i) Institution X, which keeps its books on the basis of the calendar year, has surplus, reserves, and undivided profits of \$800,000 as of January 1, 1955, and total deposits or withdrawable accounts of \$10,000,000 as of December 31, 1955. During 1955 the institution credits \$30,000, as required by a Federal agency, to a Federal insurance reserve for the sole purpose of absorbing losses. Likewise, it credits \$25,000, as permitted by State statute, to another reserve fund for the purpose of absorbing losses. In 1955 Institution X charges \$5,000 against its bad debt reserve for losses sustained during the taxable year.

(ii) The taxable income of Institution X for the taxable year 1955, computed without regard to section 593 and without regard to any section providing for a deduction the amount of which is dependent upon the amount of taxable income, is \$200,000.

(iii) Upon the basis of the facts as stated in subdivision (i) of this example, the amount by which 12 percent of the total deposits or withdrawable accounts of Institution X at the close of taxable year 1955 exceeds the sum of such institution's surplus, undivided profits, and reserves at the beginning of the taxable year is \$400,000 (12 percent of \$10,000,000, minus \$800,000).

(iv) Institution X, therefore, may deduct, for the taxable year 1955, as an addition to a reserve for bad debts, any amount it may determine that does not exceed the lesser of the amounts determined in subdivision (ii) or (iii) of this example. That amount is \$200,000 (as determined in subdivision (ii) of this example). Since under paragraph (c) of this section, the \$30,000 credited to the reserve as required by the Federal agency and the \$25,000 credited to the reserve as permitted by the State statute are regarded as amounts credited to a reserve for bad debts account Institution X can credit an additional \$145,000 (\$200,000 minus \$55,000) to a general reserve for bad debts account at any time during the taxable year.

(v) The loss of \$5,000 charged to the bad debt reserve during the taxable year does not affect the amount of the addition to the bad debt reserve provided for in paragraph (b) of this section. It is of significance only in determining the surplus, undivided profits, and reserves of Institution X as of January 1, 1956.

Example 2. The taxable income of Institution Y for the taxable year 1955, computed without regard to the deduction under section 593 and without regard to any section providing for a deduction the amount of which is dependent upon the amount of taxable income, is determined to be \$250,000. The amount by which 12 percent of the total deposits or withdrawable accounts of Institution Y at the close of the taxable year exceeds the sum of such institution's surplus, undivided profits, and reserves at the beginning of the taxable year is \$500,000. Institution Y credits \$250,000 to its bad debt reserve in 1955. In 1957, it is determined that the correct taxable income of Institution Y for 1955, computed without regard to any deduction under section 593 and without regard to any section providing for a deduction the amount of which is dependent upon the amount of taxable income, is \$275,000 and not \$250,000. Assuming that Institution Y credits the additional \$25,000 to its bad debt reserve, \$275,000 is allowable as a deduction from gross income for such institution for the taxable year 1955.

§ 1.593-2 Additions to reserve for bad debts where surplus, reserves, and undivided profits equal or exceed 12 percent of deposits or withdrawable accounts.

Where 12 percent of the total deposits or withdrawable accounts of an institution at the close of the taxable year is equal to or less than the sum of such institution's surplus, undivided profits, and reserves at the beginning of the taxable year, a reasonable addition to the reserve for bad debts as determined under the general provisions of section 166(c) may be allowable as a deduction from gross income. In making such determination, there shall be taken into account (a) surplus or bad debt reserves existing at the close of December 31, 1951 (i.e., the amount of surplus, undivided profits, and reserves accumulated prior to January 1, 1952, and in existence at the close of December 31, 1951), and (b) changes in the surplus, undivided profits, and reserves of the institution from December 31, 1951, until the beginning of the taxable year. A deduction for an addition to the reserve

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for bad debts pursuant to this section will be authorized only in those cases where the institution proves to the satisfaction of the Commissioner that the bad debt experience of the institution warrants an addition to the reserve for bad debts in excess of that provided in paragraph (b) of § 1.593-1. For definitions, see paragraph (d) of § 1.593-1.

§ 1.593-3 Taxable years affected.

Sections 1.593-1 and 1.593-2 apply only to taxable years beginning after December 31, 1953, and ending after August 16, 1954, but before January 1, 1963, and all references to sections of the Code are to the Internal Revenue Code of 1954 before amendment by the Revenue Act of 1962. Sections 1.593-4 through 1.593-11 apply only to taxable years ending after December 31, 1962, and all references to sections of the Code are to the Internal Revenue Code of 1954 after amendment by the Revenue Act of 1962.

[T.D. 6728, 29 FR 5857, May 5, 1964]

§ 1.593-4 Organizations to which section 593 applies.

The provisions of section 593 and §§ 1.593-5 through 1.593-11 (except subsection (f) of section 593 and § 1.593-10) apply to any mutual savings bank not having capital stock represented by shares, any domestic building and loan association, and any cooperative bank without capital stock organized and operated for mutual purposes and without profit. The term *thrift institution*, as used in this section and §§ 1.593-5 through 1.593-11, refers to any such financial institution. For definition of the terms *domestic building and loan association* and *cooperative bank*, see paragraphs (19) and (32), respectively, of section 7701(a).

[T.D. 549, 43 FR 21454, May 18, 1978]

§ 1.593-5 Addition to reserves for bad debts.

(a) *Amount of addition.* As an alternative to a deduction from gross income under section 166(a) for specific debts which become worthless in whole or in part, a thrift institution is allowed a deduction under section 166(c) for a reasonable addition to a reserve for bad debts. In the case of a thrift in-

stitution, the amount of the reasonable addition to such reserve for a taxable year may not exceed:

(1) For taxable years beginning after July 11, 1969, the sum of (i) the amount determined to be the reasonable addition to the reserve for losses on nonqualifying loans, determined in the same manner as is provided with respect to additions to the reserve for losses on qualifying real property loans under paragraph (d) of § 1.593-6A (relating to the experience method), and (ii) the amount determined under § 1.593-6A to be the reasonable addition to the reserve for losses on qualifying real property loans, or

(2) For taxable years beginning before July 12, 1969, the sum of (i) the amount determined under § 1.166-4 to be the reasonable addition to the reserve for losses on nonqualifying loans, and (ii) the amount determined under § 1.593-6 to be the reasonable addition to the reserve for losses on qualifying real property loans.

(b) *Crediting to reserves required*—(1) *In general.* The amounts referred to in paragraph (a) (1) and (2) of this section must be credited, respectively, to the reserve for losses on nonqualifying loans and to the reserve for losses on qualifying real property loans by the close of the taxable year, or as soon as practicable thereafter. For rules with respect to accounting for such reserves see paragraph (a)(2) of § 1.593-7.

(2) *Subsequent adjustments.* If an adjustment with respect to the income tax return for a taxable year is made, and if such adjustment (whether initiated by the taxpayer or the Commissioner) has the effect of permitting an increase, or requiring a reduction, in the amount claimed on such return as an addition to the reserve for losses on nonqualifying loans or to the reserve for losses on qualifying real property loans, then the amount initially credited to such reserve for such year pursuant to subparagraph (1) of this paragraph may have to be increased or decreased, as the case may be, to the extent necessary to reflect such adjustment.